First Quarter Financial Report 2013-14

For the period ended June 30, 2013

Farm Credit Canada
Advancing the business of agriculture

Canada

Farm Credit Canada

Headquartered in Regina, Saskatchewan, Farm Credit Canada (FCC) is a financially self-sustaining federal Crown corporation reporting to Parliament through the Minister of Agriculture and Agri-Food. We serve Canadian agriculture by providing financing and other services to more than 100,000 primary producers, value-added operators, suppliers and processors along the agriculture value chain. Operating out of 100 offices located primarily in rural communities, our more than 1,600 employees are passionate about the business of agriculture. Every year, FCC provides learning events to over 10,000 participants and knowledge publications to more than 100,000 subscribers.

Contact Corporate Communication at communications@fcc-fac.ca for more information.

First Quarter Financial Report 2013-14
For the period ended June 30, 2013

This report was prepared in accordance with the Treasury Board of Canada Standard on Quarterly Financial Reports for Crown Corporations and should be read in conjunction with disclosures and information contained in FCC's annual report and corporate plan summary.[1]

Financial results

FCC is committed to fiscal prudence and transparency. This document contains the corporation's unaudited financial results for the first quarter, which ended June 30, 2013. The corporation is on track to meet the performance measures for the current fiscal year as outlined in the Corporate Plan Summary for 2013-18.

Net income overview

($ millions)

	Three months ended	
	June 30, 2013	June 30, 2012 Restated
Net interest income	**$ 217.9**	$ 209.4
Provision for credit losses	**0.8**	(24.2)
Insurance and other income	**4.1**	3.6
Administration expenses	**(87.7)**	(80.0)
Fair value adjustment	**3.4**	(1.0)
Net income	**$ 138.5**	$ 107.8

In the first quarter of 2013-14, net income was $30.7 million higher than the same quarter in 2012-13. This was mainly due to a decrease in the provision for credit losses of $25.0 million and higher net interest income of $8.5 million, partially offset by an increase in administration expenses of $7.7 million.

The provision for credit losses for the three-month period ended June 30, 2013 decreased $25.0 million over the prior year. In the first quarter of 2013-14, an improvement in portfolio health resulted in a decrease in the required allowance for credit losses, partially offset by portfolio growth. The decrease in the required allowance resulted in a negative charge to the provision for credit losses.

Net interest income for the three-month period ended June 30, 2013 increased due to portfolio growth, partially offset by lower margins. The net interest margin for the three-month period ended June 30, 2013 decreased to 3.34% from 3.45% for the comparable period in 2012-13. The decrease in the net interest margin for the three-month period was mainly due to increased borrowing costs.

Administration expenses increased $7.7 million year-over-year, mainly as a result of salary and benefit expenses, with the largest driver being higher pension expense.

[1] These documents are available at www.fcc-fac.ca/About Us/Corporate Profile.

Loans receivable

FCC experienced overall growth in loans receivable of $0.7 billion from March 31, 2013, bringing its loan portfolio to $25.9 billion at June 30, 2013. Loan portfolio growth of 2.9% for the three months ended June 30, 2013 was lower than the loan portfolio growth of 4.5% for the first three months of the prior fiscal year.

The rate of loan portfolio growth for the three-month period ended June 30, 2013, decreased over the comparable period in 2012-13 due to lower net disbursement levels. Net disbursements for the three months ended June 30, 2013 were $2.4 billion, a decrease of $108.7 million, or 4.4%, from the three months ended June 30, 2012.

Cash flow

Cash and cash equivalents at June 30, 2013 increased to $844.5 million from $780.3 million at June 30, 2012. For the three-month period ended June 30, 2013, cash of $585.9 million was used in operating activities, $83.0 million was used in investing activities while $594.1 million was provided by financing activities.

Outlook against corporate plan summary

FCC is projected to meet all year-end financial targets as outlined in the Corporate Plan Summary for 2013-18.

Measure	Outlook
Net income	**On track** with Corporate Plan.
Return on equity	**On track** with Corporate Plan.
Efficiency ratio	**On track** with Corporate Plan.
Capital adequacy	**On track** with Corporate Plan.

Enterprise risk management

FCC has adopted an enterprise risk management framework to manage risks efficiently, consistently and in a coordinated manner. The corporation is exposed to six main categories of risk: credit, market, liquidity, operational, strategic and reputation.

FCC's risk assessment process includes risk identification and assessment, measurement, control, monitoring and reporting. This is an ongoing process for credit and market risk. All risks are assessed annually during the strategic planning process and constitute the corporation's risk profile. Executive Management Team members are responsible for developing and implementing risk management strategies and action plans to mitigate the corporation's top risks.

The FCC Board of Directors oversees the corporation's risk governance framework, which is supported by policies and committees that guide corporate decision-making.

In March 2013, FCC's Board of Directors approved a risk appetite statement that establishes the amount of risk the corporation is willing to take, avoid and accept. Following the approval of the risk appetite statement, the Board approved a series of risk policies that govern all major categories of risk to which FCC is exposed.

In April 2013, the CEO announced the creation of a Chief Risk Officer position, effective July 1. Key accountabilities include responsibility for the Enterprise Risk Management and Credit Risk business units.

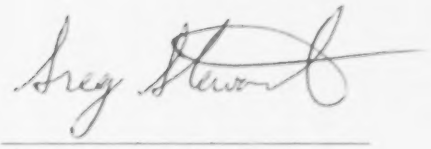
During the first quarter the Corporation received the final report from the Office of the Superintendent of Financial Institutions (OSFI) on corporate risks and risk management practices. Work is underway to address the report recommendations and further enhance FCC's risk management practices.

There were no material risks identified in the first quarter of 2013-14. It is not yet clear how the severe flooding in Alberta at the end of June will impact FCC customers and the corporation.

Statement of management responsibility

Management is responsible for the preparation and fair presentation of these consolidated quarterly financial statements in accordance with the Treasury Board of Canada Standard on Quarterly Financial Reports for Crown Corporations, and for such internal controls as management determines is necessary to enable the preparation of consolidated quarterly financial statements that are free from material misstatement. Management is also responsible for ensuring that all other information in this quarterly report is consistent, where appropriate, with the consolidated quarterly financial statements.

Based on our knowledge, these unaudited consolidated quarterly financial statements present fairly, in all material respects, the financial position, results of operations and cash flows of the corporation, as at the date of and for the periods presented in the consolidated quarterly financial statements.



Greg Stewart, P.Ag., C.Dir.
President and Chief Executive Officer

Rick Hoffman, CMA, MBA
Executive Vice-President and Chief Financial Officer

Regina, Canada
August 15, 2013

Condensed Consolidated Financial Statements
Consolidated Balance Sheet

(Unaudited)
(Thousands of Canadian dollars)

	June 30, 2013	March 31, 2013 Restated Note 1	April 1, 2012 Restated Note 1
Assets			
Cash and cash equivalents	$ 844,461	$ 917,871	$ 904,217
Temporary investments	233,530	164,781	83,813
Accounts receivable	15,786	18,666	16,356
Derivative financial assets	54,885	71,183	67,898
	1,148,662	1,172,501	1,072,284
Loans receivable – net (Notes 2 and 3)	25,217,363	24,493,332	22,580,309
Finance leases receivable – net	13,128	12,908	9,541
Venture capital investments	77,839	73,366	53,527
	25,308,330	24,579,606	22,643,377
Equipment and leasehold improvements	22,098	23,467	26,655
Computer software	36,720	38,329	40,091
Equipment under operating leases	45,248	40,086	28,331
Other assets	18,321	16,825	18,307
	122,387	118,707	113,384
Total assets	$ 26,579,379	$ 25,870,814	$ 23,829,045
Liabilities			
Accounts payable and accrued liabilities	$ 62,484	$ 57,459	$ 59,675
Derivative financial liabilities	-	-	84
	62,484	57,459	59,759
Borrowings (Note 4)			
Short-term debt	11,362,936	10,045,902	9,568,666
Long-term debt	11,174,931	11,906,034	10,772,729
	22,537,867	21,951,936	20,341,395
Transition loan liability	91,061	92,499	84,108
Retirement benefit liabilities	226,137	225,601	224,461
Other liabilities	12,500	12,129	11,550
	329,698	330,229	320,119
Total liabilities	22,930,049	22,339,624	20,721,273
Equity			
Contributed surplus	547,725	547,725	547,725
Retained earnings	2,909,175	2,770,326	2,340,412
Accumulated other comprehensive income	162,049	184,752	203,477
Equity attributable to shareholder of parent entity	3,618,949	3,502,803	3,091,614
Non-controlling interest in special purpose entity	30,381	28,387	16,158
	3,649,330	3,531,190	3,107,772
Total liabilities and equity	$ 26,579,379	$ 25,870,814	$ 23,829,045

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Operations

(Unaudited)
(Thousands of Canadian dollars)

	Three months ended	
	June 30, 2013	June 30, 2012 Restated Note 1
Interest income	$ 285,810	$ 272,443
Interest expense	67,929	62,999
Net interest income	217,881	209,444
Provision for credit losses	(836)	24,185
Net interest income after provision for credit losses	218,717	185,259
Net insurance income	3,598	3,308
Other income	501	272
Net interest income and non-interest income	222,816	188,839
Administration expenses		
Salary expense	38,468	33,921
Benefits expense	19,016	16,403
Professional fees expense	8,057	8,485
Facilities, software and equipment expense	6,535	6,071
Amortization and depreciation expense	8,106	6,596
Travel and training expense	3,470	3,284
Marketing and promotion expense	1,175	1,090
Other expenses	2,837	4,186
Total administration expenses	87,664	80,036
Net income before fair value adjustment	135,152	108,803
Fair value adjustment	3,384	(968)
Net income	$ 138,536	$ 107,835
Net income (loss) attributable to:		
Shareholder of parent entity	$ 138,849	$ 107,913
Non-controlling interest in special purpose entity	(313)	(78)

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Comprehensive Income

(Unaudited)
(Thousands of Canadian dollars)

	Three months ended	
	June 30, 2013	June 30, 2012 Restated Note 1
Net income	**$ 138,536**	$ 107,835
Other comprehensive income		
Items that are or may be reclassified to net income		
Net (losses) gains on derivatives designated as cash flow hedges	**(17,235)**	8,316
Transfer of net realized gains on derivatives designated as cash flow hedges to net income	**(5,650)**	(5,660)
Net unrealized gains (losses) on available-for-sale financial assets	**182**	(21)
	(22,703)	2,635
Total other comprehensive (loss) income	**$ (22,703)**	$ 2,635
Total comprehensive income	**$ 115,833**	$ 110,470
Total comprehensive income (loss) attributable to:		
Shareholder of parent entity	**$ 116,146**	$ 110,548
Non-controlling interest in special purpose entity	**(313)**	(78)

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Changes in Equity

(Unaudited)
(Thousands of Canadian dollars)

	Balance April 1, 2013 Restated Note 1	Net income	Other comprehensive income	Distributions to non-controlling interest	**Balance June 30, 2013**
Contributed surplus	$ 547,725	$ -	$ -	$ -	**$ 547,725**
Retained earnings	2,770,326	138,849	-	-	**2,909,175**
Net gains (losses) on derivatives designated as cash flow hedges	185,072	-	(22,885)	-	**162,187**
Net unrealized (losses) gains on available-for-sale financial assets	(320)	-	182	-	**(138)**
Total accumulated other comprehensive income (loss)	184,752	-	(22,703)	-	**162,049**
Total equity attributable to parent	3,502,803	138,849	(22,703)	-	**3,618,949**
Non-controlling interest in special purpose entity	28,387	(313)	-	2,307	**30,381**
Total	$ 3,531,190	$ 138,536	$ (22,703)	$ 2,307	**$ 3,649,330**

(Unaudited)
(Thousands of Canadian dollars)

	Balance April 1, 2012 Restated Note 1	Net income Restated Note 1	Other comprehensive income	Distributions to non-controlling interest	Balance June 30, 2012 Restated Note 1
Contributed surplus	$ 547,725	$ -	$ -	$ -	$ 547,725
Retained earnings	2,340,412	107,913	-	-	2,448,325
Net gains on derivatives designated as cash flow hedges	204,045	-	2,656	-	206,701
Net unrealized losses on available-for-sale financial assets	(568)	-	(21)	-	(589)
Total accumulated other comprehensive income	203,477	-	2,635	-	206,112
Total equity attributable to parent	3,091,614	107,913	2,635	-	3,202,162
Non-controlling interest in special purpose entity	16,158	(78)	-	34	16,114
Total	$ 3,107,772	$ 107,835	$ 2,635	$ 34	$ 3,218,276

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Cash Flows

(Unaudited)
(Thousands of Canadian dollars)

	Three months ended	
	June 30, 2013	June 30, 2012 Restated Note 1
Operating activities		
Net income	**$ 138,849**	$ 107,913
Adjustments to determine net cash (used in) provided by operating activities:		
Net interest income	**(217,881)**	(209,444)
Unwind adjustment on impaired loans	**(552)**	260
Provision for credit losses	**(836)**	24,185
Fair value adjustment	**(3,384)**	968
Depreciation and amortization	**8,106**	(6,596)
Other	**(1,741)**	(1,589)
Net cash outflow from loans receivable	**(736,686)**	(1,054,081)
Net cash outflow from finance leases receivable	**(40)**	(1,213)
Net change in other operating assets and liabilities	**11,668**	22,229
Interest received	**291,460**	292,180
Interest paid	**(74,831)**	(73,786)
Cash used in operating activities	**$ (585,868)**	$ (898,974)
Investing activities		
Net cash outflow from temporary investments	**$ (68,641)**	$ (225,439)
Acquisition of venture capital investments	**(4,127)**	(2,907)
Proceeds on disposal and repayment of venture capital investments	**115**	7
Purchase of equipment and leasehold improvements	**(1,286)**	(1,612)
Purchase of computer software	**(1,562)**	(2,874)
Purchase of equipment under operating leases	**(7,460)**	(5,061)
Disposal of real estate property held for sale	**-**	100
Cash used in investing activities	**$ (82,961)**	$ (237,786)
Financing activities		
Long-term debt issued	**$ 434,000**	$ 1,605,018
Long-term debt repaid	**(1,471,000)**	(1,121,254)
Short-term debt issued	**9,363,302**	8,446,807
Short-term debt repaid	**(7,732,175)**	(7,918,151)
Cash provided by financing activities	**$ 594,127**	$ 1,012,420
Change in cash and cash equivalents	**$ (74,702)**	$ (124,340)
Cash and cash equivalents, beginning of period	**917,871**	904,217
Effects of exchange rate changes on the balances of cash held and due in foreign currencies	**1,292**	410
Cash and cash equivalents, end of period	**$ 844,461**	$ 780,287
Cash and cash equivalents are comprised of:		
Cash	**$ 102,912**	$ 67,949
Short-term investments	**741,549**	712,338

The accompanying notes are an integral part of the condensed consolidated financial statements.

Notes to the Condensed Consolidated Financial Statements (Unaudited)

1. Significant accounting policies

Basis of presentation

Condensed consolidated interim financial statements (interim financial statements) comply with the Standard on Quarterly Financial Reports for Crown Corporations issued by the Treasury Board of Canada.

These interim financial statements do not include all of the information required for complete annual financial statements and should be read in conjunction with the annual, audited financial statements for the year ended March 31, 2013.

Unless otherwise stated, all dollar amounts presented in the Notes to the Condensed Consolidated Financial Statements are in thousands of Canadian dollars, which is the functional currency of the corporation.

Accounting policies

The accounting policies adopted in the preparation of these interim financial statements are consistent with those followed in the annual, audited financial statements for the year ended March 31, 2013, except as described below.

New and amended accounting policies

The International Accounting Standards Board (IASB) has issued a number of new standards, interpretations, amendments and improvements. The standards that are relevant to FCC are listed below. They are effective April 1, 2013.

New standards include:

- IFRS 10 – Consolidated Financial Statements replaces the guidance on control and consolidation in IAS 27 – Consolidated and Separate Financial Statements, and SIC-12 – Consolidation: Special Purpose Entities. IFRS 10 requires consolidation of an investee only if the investor has power over the investee, exposure to variable returns from its involvement with the investee and the ability to use its power over the investee to affect its returns. IFRS 10 provides detailed guidance on applying the definition of control. The accounting requirements for consolidation have remained consistent with IAS 27. The corporation assessed its consolidation conclusions and determined IFRS 10, which was adopted on April 1, 2013, did not change the consolidation status of its subsidiaries and investees. While Avrio Ventures Limited Partnership (Avrio Fund I), Avrio Ventures Limited Partnership II (Avrio Fund II) and Avrio Subordinated Debt Limited Partnership (Avrio Subordinated Debt Fund) are no longer special purpose entities with the removal of SIC-12, the corporation will continue to consolidate them given that it is entitled to and exposed to a majority of the benefits and risks.
- IFRS 12 – Disclosure of Interests in Other Entities outlines the disclosure requirements for all forms of interest in other entities, both on and off the balance sheet. FCC has assessed the disclosure requirements and determined that the adoption of IFRS 12 did not require additional disclosure in its interim financial statements.

- IFRS 13 – Fair Value Measurement provides a single framework for measuring fair value. The measurement of an asset or liability's fair value is based on assumptions that market participants would use when pricing the asset or liability under current market conditions, including assumptions about risk. FCC adopted IFRS 13 on April 1, 2013, on a prospective basis. The adoption of IFRS 13 did not require any adjustments to the valuation techniques used by FCC to measure fair value and did not result in any measurement adjustments as at April 1, 2013. The corporation will provide additional disclosures required by IFRS 13 in the annual financial statements for the year ended March 31, 2014.

Amended standards include:

- IAS 1 – Presentation of Financial Statements requires the corporation to group other comprehensive income items by those that will be reclassified to income and those that will not. The corporation has reclassified comprehensive income items of the comparative periods. These changes did not result in any adjustments to other comprehensive income or comprehensive income.
- IAS 19 – Employee Benefits was amended to improve the recognition, presentation and disclosure of defined benefit plans. The amendments introduce a calculation for net interest costs, which will be included in benefits expense. Under the net interest method, plan assets are multiplied by the same discount rate used to calculate the interest expense on the defined benefit liability to determine the interest income on the plan assets. This differs from the previous methodology, which used the expected rate of return. Under the previous standard, fair value is the full value of the refundable tax assets. Under the new standard, the fair value of refundable tax assets will be calculated as the present value of future reimbursements. This amendment was implemented effective April 1, 2013, and applied retrospectively. The transition adjustment reduced pension assets and opening retained earnings at March 31, 2013 by $7.5 million. The decrease in pension assets increased retirement benefit liabilities. In addition, for the year ended March 31, 2013, the retrospective application of the standard increased pension expense by $9.8 million and increased other comprehensive income by $8.9 million. The corporation will provide additional disclosures required by IAS 19 in the annual financial statements for the year ended March 31, 2014.

Accounting standards issued but not yet effective

The corporation has reviewed the new standards, amendments and interpretations that have been issued by the International Accounting Standards Board (IASB) or the International Financial Reporting Interpretations Committee (IFRIC), but are not yet effective, and has determined that the following may have an impact on it. Management is assessing the impact of these standards and amendments on the corporation's financial statements and accounting policies.

Standard	Details	Date of initial application
IAS 32 – Financial Instruments: Presentation	The amended standard was issued together with the amended IFRS 7 – Financial Instruments: Disclosures to clarify the guidance on offsetting financial assets and liabilities. It is anticipated that this standard will result in increased disclosure only.	April 1, 2014
IFRS 9 – Financial Instruments	The new standard provides requirements for classifying and measuring financial assets and liabilities. This standard is the first in a three-phase project in progress by the IASB to replace IAS 39 – Financial Instruments: Recognition and Measurement in its entirety. It is anticipated that this standard will change the classification of the corporation's temporary investments from available for sale (AFS) to fair value through profit and loss.	April 1, 2015

2. Loans receivable – net

($ thousands)

	Term to maturity				
	Within 1 year	1 - 5 years	Over 5 years	June 30, 2013	March 31, 2013
Floating	$ 3,116,760	$ 12,306,968	$ 798,490	$ 16,222,218	$ 15,747,663
Fixed	1,409,074	5,614,929	2,301,171	9,325,174	9,086,081
Performing loans	4,525,834	17,921,897	3,099,661	25,547,392	24,833,744
Impaired loans				328,178	321,209
Deferred loan fees				(21,456)	(21,618)
Loans receivable – gross				25,854,114	25,133,335
Allowance for credit losses				(636,751)	(640,003)
Loans receivable – net				$ 25,217,363	$ 24,493,332

3. Allowance for credit losses – loans receivable

($ thousands)

	June 30, 2013	March 31, 2013
Individual allowance, beginning of year	$ 151,012	$ 140,800
Provision for credit losses	17,716	31,476
Losses covered under the Hog Industry Loan Loss Reserve Program	(259)	9,391
Unwind adjustment on impaired loans	(552)	3,200
Write-offs	(743)	(35,602)
Recoveries	189	1,747
Individual allowance, end of period	$ 167,363	$ 151,012
Collective allowance, beginning of year	$ 488,991	$ 481,150
Provision for credit losses	(18,554)	6,571
Losses covered under the Hog Industry Loan Loss Reserve Program	(967)	3,552
Write-offs	(163)	(2,451)
Recoveries	81	169
Collective allowance, end of period	$ 469,388	$ 488,991
Total allowance	$ 636,751	$ 640,003

4. Borrowings

Short-term debt

($ thousands)

		June 30, 2013		March 31, 2013
Government of Canada debt	$	**11,196,076**	$	9,771,040
U.S. dollar fixed-rate promissory notes		**116,530**		115,105
Retail and institutional fixed-rate notes		**50,129**		152,153
Structured note index-linked		**199**		198
Cash collateral due to derivative counterparties		**2**		7,406
Total	$	**11,362,936**	$	10,045,902

Long-term debt

($ thousands)

		June 30, 2013		March 31, 2013
Government of Canada debt	$	**10,763,126**	$	11,490,130
Retail and institutional fixed-rate notes		**411,805**		415,904
Total	$	**11,174,931**	$	11,906,034

The corporation enters into borrowings with the Government of Canada through the Crown Borrowing Program. Interest accrued and incurred on these borrowings is recorded in borrowings and interest expense, respectively. The Government of Canada interest expense recorded to June 30, 2013, was $58.8 million (June 30, 2012 - $54.0 million).